



MINUTES
Uniformity Committee and Subcommittee Meetings
Hotel Monteleone
214 Royal Street
New Orleans, Louisiana 70130-2201
November 5-6, 2007

I. Welcome and Introductions

The following individuals attended one or more of the meetings of the Sales/Use Tax Subcommittee, the Income/Franchise Subcommittee, or the Full Uniformity Committee:

Name	Affiliation	Name	Affiliation
Ted Spangler	ID	Wood Miller	MO
Richard Cram	KS	Danny Walker	AR
Carol Ireland	KS	Charla Wagner	KS
Joe Thomas	CT	Janielle Lipscomb	OR
Lennie Collins	NC	John Kutsukos	CT
Andrew Glancy	WV	Leonore Heavey	LA
Jan Bianchi	WA	Frank Hales	UT
Rod Marrelli	UT	Brenda Gilmer	MT
Michael Fatale	MA	Nancy Prosser	TX
Heidi Chowning	NM	Rebecca Abbo	NM
Dan Armen	NM	Charles Wilson	DC
Tammy Sorenson	CO	Randy Tilley	ID
Robynn Wilson	AK	Cathy Wicks	MN
Beth Cooley	COST	Todd Lard	COST
Keith Getschel	MN	Mike Mason	AL
Christy Vandevarder	AL	Mary Loftsgard	ND
Dee Wald	ND	Reva Tisdale	ID
Eugene Walborn	MT	Lee Baerlocher	MT
Dianne Smith	Sutherland Asbill	Dana Bernstein	NAREIT
Deborah Bierbaum	AT&T	Eric Smith	OR
Dan Armer	NM	Marianick Simon	General Electric
Ben Miller	CA-FTB		
MTC Staff			
Elliott Dubin	Sheldon Laskin	Ted Jutras	Roxanne Bland
Joe Huddleston	Shirley Sicilian	Bruce Fort	Jeff Silver
Ken Beier	Les Koenig		

Sales and Use Tax Uniformity Subcommittee
Monday, November 5, 2007
1:00 PM – 5:00 PM

II. Public Comment Period

No public comment was offered at this time.

III. Reports and Updates

Roxanne Bland, MTC Counsel, reported on Executive Committee and Commission action on uniformity proposals. She also reported on federal issues affecting state taxation, including Streamlined Sales Tax Legislation, Internet Tax Freedom Act and Hotel Intermediaries/Car Rentals Legislation.

IV. Hotel Intermediaries Project

Richard Cram, Chair, summarized the drafting group's proposal for the Committee. The Committee asked whether the proposal would include certain travel arrangements in the tax base, such as time share arrangements. Ted Spangler suggested the proposal should not address the scope of taxable arrangements. Rather, the scope of arrangements subject to tax should be left "as is" in each jurisdiction.

The Committee discussed problems with travel agents. Travel agent fees are not subject to tax in most states. Brenda Gilmer noted the Montana model, which taxes the full amount of the transaction unless a separate charge is identified to the customer as a service charge. Robyn Wilson suggested that the Montana model would be a departure from the approach being taken currently by the drafting group and asked why the Committee should deviate from the current model. Mr. Cram identified problems with the current model's dual remittance structure which would require an intermediary to remit to a hotel and a hotel to then remit to the state or local government. Michael Fatale noted that legislation introduced in Massachusetts takes the same approach as Montana. Mr. Cram suggested the drafting group should take a look at the Montana and Massachusetts model and report back to the Committee. Ms. Gilmer and Mr. Fatale offered to e-mail a copy of their legislation to Roxanne Bland.

On the issue of aggregate charges, Mr. Cram suggested the language from SST on telecommunications bundling might be a better formula.

Rod Marrelli asked that we have a white board available at the next meeting.

V. Model Sampling Authorization Statute and Regulation

A. Presentation by Harold Jennings, MTC

Mr. Jennings expressed the view that, while he agreed with most of the hearing officer's recommendations, he does not agree that the term "reasonable" should be used in the statute to determine when the use of statistical sampling is appropriate in an audit. Mr. Jennings is of the view that the term "reasonable" is too subjective to be defined by

regulation. Mr. Jennings would substitute “when statistical sampling is not possible or when the circumstances of the audit dictate that alternative sampling methods would be a better use of department resources” (e.g., too time consuming to retrieve records to conduct statistical sampling). For similar reasons, Mr. Jennings recommends that Section 2a of the proposed regulation be eliminated.

B. Review of Hearing Officer Recommendations

The Hearing Officer’s first recommended change to the proposal is to create a new Section 1 that defines the judgmental, probability and statistical sampling techniques. The definitions for judgmental and probability sampling techniques were taken from (Freund and Williams, *Dictionary/Outline of Basic Statistics*, Dover Publications, 1991), and the definition for statistical sampling from the International Standards on Auditing 530 developed by the International Federation of Accountants.¹

The Hearing Officer’s second recommended change is that Section 2, regarding when the use of sampling techniques is appropriate, be revamped in its entirety. Rather than vague terms like “voluminous” or “insufficient”, section 2 would provide a mathematical criteria for determining when the use of audit sampling techniques is appropriate, and further provides a procedure for the department to follow in initiating the use of such techniques.

On referral back to the Committee, the Hearing Officer suggests that the Committee consider the following questions:

1. As a general matter, does the Committee believe that the revised proposal reflects the intent of the original? If not, should the original intent be reconsidered or should the proposal be revised? Recall that the Uniformity Committee was originally requested by the Audit Committee to craft a model statistical sampling authorization statute. In the course of its deliberations, the Uniformity Committee decided to expand the scope of its mandate to include other types of common sampling techniques, and further decided to expand the scope of the project to include the development of a model regulation to accompany the model statute.
2. Section 1, Definitions—should a definition for the random sampling technique be included?
3. If the judgmental sampling technique is of limited evidentiary value in a judicial/quasi-judicial proceeding contesting audit results, should these nevertheless be included? Should their use be limited to certain situations?

The hearing officer submitted a revised proposed statute and regulation to reflect the recommendations made in her memorandum to the Uniformity Sales and Use Tax Committee.

¹ <http://www.taxadmin.org/fta/pub/sample.pdf>

D. Committee Discussion

Ted Spangler commented that there is a philosophical problem reflected in COST's objection to allowing state revenue departments unlimited discretion to contest the state's selection of the audit technique. More and more taxpayers are challenging audit techniques. Mr. Spangler is troubled by the statute's use of the term "reasonable" as going too far in giving the taxpayer too much authority in controlling how the audit will be conducted. Mr. Spangler does not like Reg. 2a for the same reason.

Brenda Gilmer suggested striking "when examining returns or records" from the introductory language of the statute. Ms. Gilmer noted that the purpose of statistical sampling is to facilitate assessments, not to examine books and records. Mr. Spangler questioned whether this is a distinction without a difference.

Rod Morelli suggested striking all statutory language after the authorized sampling techniques. Mr. Spangler said the subcommittee's intent was to put some limit on the revenue department's discretion to use statistical sampling. Mr. Spangler indicated that it would be insufficient for a taxpayer to show that a different method would reach a proper result. Mr. Spangler would require the taxpayer to show what that proper result would be. The revenue department would then have the burden to defend what it had done, or show that the taxpayer's result is less reasonable. Mr. Spangler noted that courts use concepts of reasonableness all the time.

Mr. Morelli moved that all the language after "or other sampling techniques" be stricken from the proposed statute and that Section 2 of the proposed regulation be stricken in its entirety. Jan Bianchi seconded the motion, which carried.

VI. Possible Telecommunications Transactions Project

Roxanne Bland summarized the proposed project to draft statutes that could serve as models of best practices for administration of telecommunications transaction taxes under different state administrative structures with varying degrees of centralization. She also summarized the materials provided to the Committee, including legislation from Florida, Utah and Virginia. Deborah Bierbaum, AT&T, spoke in favor of initiating a project. Ms. Bierbaum suggested South Carolina legislation would also be a possible model. Mr. Cram suggests taking up one model focused on state level administration. Ms. Bierbaum noted class action protections are already written into the streamlined legislation and in the Mobile Telecommunications Sourcing Act. This proposal would assist states if the streamlined proposal passes and it becomes necessary for states to set up distribution formulas and other central administration tasks that are not covered in SSTP (or for those that are not doing streamlined).

Mr. Spangler voiced concern with the idea that MTC develop a model distribution formula for states. This is not something MTC proposals have dealt with in the past and would arouse state specific sensitivities. Ms. Bierbaum clarified that what she had in

mind was more to provide an array of best practices for various levels of centralization. On that particular level of centralization noted by Mr. Spangler, what she had in mind was more the Virginia model. The idea is to identify for the states what the considerations are that need to be stated in statute. The idea is not to have uniformity in distribution formula, but just to identify that there must be a formula. The models would be “shells” to help solve that drafting problem. They would be tools for states to feel comfortable that there is language they can use if streamlined is enacted by congress. States would not have years to come up with SST conforming structures if SST passes. This is not a uniformity focus, but an administrative focus. The models could cover many telecommunication taxes. Not all taxes would come under one approach even within a single state.

Mr. Spangler moved the subcommittee take up the project and assign MTC staff to work with representatives of industry and bring to subcommittee 2 or 3 draft models from which the Subcommittee could then begin a discussion. Carol Ireland seconded and the motion passed 9 in favor, 2 abstentions, no opposed.

VII. Discussion of Nexus Committee Request to Establish Uniform Timelines for Duration of Nexus

Mr. Laskin noted that as the result of a survey undertaken by the MTC Nexus Committee in March 2007 on the states’ varied practices in determining the duration of taxpayer nexus, that Committee has requested that the subcommittee consider a project to develop a uniform rule to address the issue. After a short discussion, the subcommittee voted by voice vote not to take up the request.

VIII. New Business

There was no new business before the subcommittee.

IX. Adjourn

The subcommittee voted to adjourn.

*Income and Franchise Tax Uniformity Subcommittee
Tuesday November 6, 2007
9:00 AM—2:30 PM*

I. Welcome and Introductions

II. Public Comment Period

No public comment was received at this time.

III. Reports and Updates

Sheldon Laskin, MTC Counsel, gave a status report on the public hearing on the proposed model regulation for apportionment of income from the sale of telecommunications and ancillary services.

Bruce Fort, MTC Counsel, gave a status reported on the public hearing on proposed model statute for taxation of captive real estate investment trusts.

Ms. Bland reported on federal issues affecting state taxation including Business Activity Tax Legislation.

Shirley Sicilian, MTC General Counsel, reported on the MTC project to recommend modifications to the Multistate Tax Compact Article IV, §17. She also reported on our work with NCCUSL on this effort.

IV. Report on Amendments to MTC Model Financial Institutions Apportionment Statute/Regulation Project

The Executive Committee directed the Uniformity Committee to amend this Model regulation at the Annual Meeting, July 2007. A meeting for interested parties and state representatives was held on November 9 at the Hotel Monteleone to prioritize the issues. The group debated which process would work best. Ted Spangler preferred an iterative process in which the working group – MTC staff and industry representatives – would report to the Uniformity Committee after each step for feedback. Dee Wald (ND) stated that the working group should state the policy goals first. The income tax uniformity subcommittee agreed that the process should be iterative, rather than having the working group present a fully-developed model to the subcommittee.

V. Regulated Investment Company Project

Bruce Fort, MTC Counsel reported that the Committee decided, at the November 2006 meeting, to separate RIC and REIT issues into two separate model statutes, but be maintained as a single MTC project.. Mr. Fort explained that captive RICs could be used for income shifting because the RIC is entitled to a dividends-paid deduction under federal law, but the dividends may be paid to related shareholders that are either exempt from inclusion in the combined return in combined filing states (e.g., captive insurance companies or 80/20 companies), or beyond the reach of separate filing states. The income can then be returned to the taxpayer either as a non-taxed ordinary domestic dividend or as a loan. Mr. Fort suggested that the approach taken for captive REITs--denial of the dividends-paid deduction--could be ineffective for separate filing states because the captive RIC may lack nexus in any state beyond its commercial domicile. Mr. Fort suggested that the only approach which appears to be workable for separate-filing states would be to deny the dividends-paid deduction and to force a combination with entities doing business in those states.

For combined filing states, the current captive REIT model should be effective.

The REIT drafting committee consisting of Joe Garrett (AL), Reba Tisdale (ID), Kim Ferrell (UT), Carl Joseph (CA) and Lennie Collins (NC) will continue working on this RIC project. Ms. Tisdale recommended that the group look at the revision of the financial institution regulation. Brenda Gilmer (MT) that the group should provide a good description of the problem. There was no public comment.

VI. UDITPA §18—Clarifying “Rare and Unusual Circumstances”

Mr. Fort noted that the Commission regulation governing the application of Section 18 provides that states may employ it only under “rare and unusual circumstances.” Determining just what circumstances are “rare and unusual” enough to invoke the application of Section 18 has spawned a great deal of litigation. He noted his recent speaking engagement at (Hartman), wherein it was noted that tax administrators almost never invoke the provisions of Section 18, and that when taxpayers request its application, tax administrators usually turn them down. As UDITPA gets more and more outdated, there is no question that tax administrators will receive more and more requests to apply Section 18. Mr. Fort guided the subcommittee through a draft list of issues that should be considered in working on this project, such as whether the current Section 18 provides tax administrators with the flexibility to address new types of business activities or structures that do not fit well within the general apportionment statutes and regulations. He noted that of all of the items on this list, the most important is that the subcommittee form a drafting group for this project. Mr. Spangler questioned that with respect to Issue #7 (should any amendment of Section 18 await proposed changes to UDITPA) whether it would be better for the subcommittee to wait until NCCUSL finishes its work with that model statute. Mr. Fort disagreed, noting that it was the MTC who approached NCCUSL and advised that it would proceed with its efforts to revise UDITPA should that body decide to undertake its own revisions. This way, the MTC can develop and submit proposals to NCCUSL as recommended changes from the states. In addition, if NCCUSL develops an amendment that is unacceptable to the states, states need to have alternatives available. Ms. Sicilian reminded the group that the NCCUSL project is for amendments to a statute; while this project, at this point, is focused on amendments to the regulation for that statute.

Janielle Lipscomb, OR, noting the breadth of the extensive list of issues presented by MTC staff, questioned what, exactly, is the problem that the committee is attempting to resolve. Mr. Fort responded that tax administrators have invoked Section 18 for purposes of combating the use of tax planning tools like churning Treasury functions, etc. The point is that tax administrators have been using the regulation to stop distortion, not in those “rare and unusual circumstances” for which the regulation provides. Though courts, in interpreting Section 18 have held for the states in these cases, those victories were narrowly won. The question is how Section 18’s language can be amended to reflect the breadth of circumstances in which a tax administrator might want to invoke the section. For example, the language could be amended to reflect the factors test adopted by the Oregon courts in its Twentieth-Century Fox litigation. The regulation could also be amended by deleting the phrase “rare and unusual.” The bottom line is that if the language is not addressed, states run the greater danger of losing a case where Section 18 is invoked.

Mr. Spangler noted that it would seem that the goal of this project is not to address all sorts of different taxpayers, but to remove the apparent limitation on tax administrators to address the circumstances under which tax administrators can invoke Section 18. Section 18 should recognize that tax administrators should be able to deviate from the state’s apportionment formula as a general matter, not on a case by case basis because of

something really unusual with respect to a particular industry. Mr. Cram, KS, noted that his state has had some success in using Section 18 in cases involving captive insurance companies. He noted his interest in amending Section 18's possibly restrictive language, but would not want to go so far as amending the burden of proof.

The subcommittee formed a drafting group consisting of Wood Miller, MO (Chair), Ted Spangler, ID, Richard Cram, KS and Leonore Heavey, LA, to work on developing language to amend Section 18.

VII. Possible Project on Reporting Federal Adjustments—Expansion of Current RAR Model Language

Sheldon Laskin, MTC Counsel, informed the group that this project, if the Committee were to take it up, would form an MTC/Industry Task Force to develop a form for the states to adopt that business taxpayers would use for reporting RAR's. Todd Lard of COST and representatives of AICPA would also cooperate.

There was some discussion regarding the states' issuance of such a form. Members discussed the idea that, unlike apportionment rules, there is not necessarily uniformity in tax bases and a single form could be very difficult to create. One member noted that IT costs would rise. However, audit selection candidates are sometimes based on RAR's thus a uniform RAR may be helpful.

ND moved that the Committee should not take up this project. The Committee voted 18 yes and 1 abstention. The Committee will not take up this project.

VIII. New Business

IX. Adjourn

*Full Uniformity Committee
Tuesday, November 6, 2007
2:30 PM—5:00 PM*

I. Welcome and Introductions

II. Approval of Minutes of July 2007 Meetings

The Committee approved the minutes from the July meeting on unanimous voice vote.

III. Public Comment Period

There was no public comment.

IV. Executive Director's Report

Mr. Huddleston noted that the work of the Uniformity Committee will be instrumental in the NCCUSL project to amend Section 17 of UDITPA. He also noted the success of the MTC's audit program has led to its efforts to expand the MTC Audit Program presence

nationally. Regarding the oral argument heard by the U.S Supreme Court in *Kentucky v. Davis* (November 5, 2007; issue is the constitutionality of the states' practice of taxing interest earned on bonds issued by sister states but exempting its own), Mr. Huddleston said it was reported to him that Kentucky's arguments and the views expressed by the MTC in its amicus brief appeared to have been well received by the Justices, and that current opinion has it that it would be a surprise if Kentucky does not carry the day.

With respect to the MTC's Alternative Dispute Resolution Program, Mr. Huddleston reported that an MTC mediation was successfully concluded between a taxpayer and two member states, and further encouraged states to take advantage of the service. Finally, he noted that MTC programs and training opportunities continue to expand and that discussions are underway to possibly open a select number to the public.

(Income/Franchise Tax Segment)

V. Reports and Possible Action Items.

Wood Miller, MO (Chair) noted that the subcommittee reviewed the status and background of existing and potential projects, and noted the meeting of the Financial Institutions working group on Friday, November 9th. Regarding the project on RICs, the subcommittee charged the working group to reconvene and consider alternative approaches to this issue for subcommittee discussion. The subcommittee further formed a working group on the Section 18 project. The subcommittee voted not to take up the project on RARs. There are no recommendations or motions to bring to the full committee.

(Sales/Use Tax Segment)

VI Reports and Possible Action Items.

Richard Cram, KS (Chair), reported that with respect to the hotel intermediaries project, the drafting group will develop a third approach that will not have a dual remittance feature. The subcommittee reviewed the Hearing Officer's Report on the Model Audit Sampling Authorization Statute and Accompanying Regulation. After discussion, the subcommittee voted to amend the Regulation by deleting language addressing the appropriate use of sampling techniques and agreements between the state tax agency and the taxpayer to use such techniques, and further voted to refer the proposal as amended to the full Committee for its consideration for further referral to the Executive Committee. The subcommittee further voted to take up the project to develop model regulations concerning centralized administration of telecommunications transaction taxes. Finally, the subcommittee voted not to take up a request from the Nexus Committee to develop a uniform rule establishing the duration of nexus.

The Chair requested a motion to refer the Model Audit Authorization Statute and Accompanying Regulation, as amended, to the Executive Committee. Mr. Cram, KS, so moved, and was seconded by Mr. Mason, AL. The motion passed with 18 yeas, 0 nays and 0 abstentions.

VII. Roundtable Discussion

Members summarized their current major legislative, regulatory and legal issues.

VIII. New Business

There was no new business before the Committee.

IX. Adjourn

The Committee adjourned.